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ABSTRACT

Designed for the general public and possibly suitable also for high school economics students, this pamphlet presents a brief overview of United States currency. Separate sections discuss the role of currency today, how the dollar has evolved, how the dollar got its name, laws concerning legal tender, types of currency in circulation, the meaning of the inscriptions appearing on currency, how currency reaches the public, why the amount of currency changes, how the note issue mechanism works, how much currency is in circulation, why banks are decentralized, and who owns and operates the Federal Reserve Banks. Specific topics include the earliest monetary statute (The Mint Act), the first coin struck by the U.S. government, present laws concerning the issuing of currency, and specific denominations of Federal Reserve notes. A look at the inscription "In God We Trust," the Treasury Seal, and the Susan B. Anthony dollar is followed by an explanation of the procedure currency undergoes before it reaches the public. An explanation of the note issue mechanism, the total amount of cash in the Federal Reserve System, and the decentralization of Federal Reserve Banks is provided. In addition, the role of the Board of Governors of the Federal Reserve System, and stock ownership by commercial banks of the Federal Reserve System are discussed. (LH)

# U.S. CURRENCY

A Perspective

of

Its Role Today

# U.S. CURRENCY

## A Perspective of Its Role Today

The nucleus of any modern nation's monetary system is its currency—the cash its citizens use to do business, buy the necessities and niceties of everyday life, and settle debts among themselves or with their government. Currency—coin and paper currency—is a nation's official money provided by the government, under its sovereign power. It is distinguished from other forms of money in that it may circulate freely from person to person without need for endorsement or reference to the character or credit of the bearer.

In the United States today, currency is actually only part of what is embraced by the term *money*. Because of the size and diversity of the nation's economy, Americans carry on an estimated 90 percent of all dollar transactions with checkbook money. Even so, federal currency forms a foundation on which the rest of the monetary edifice is built.

The first currency denominated as a United States dollar was issued on October 15, 1794. In the 184 years since then, federal currency has passed through a long evolutionary process which, by and large, parallels the social, political, and economic evolution of the American nation itself.

# How the dollar has evolved

The Constitution outlines only the broadest provisions for United States money, assigning ultimate power "to coin money" and "regulate the value thereof" to the Congress. Over the years, the Congress has deliberated upon and enacted more than 60 key statutes to shape our present monetary system. And the Supreme Court has consistently upheld these congressional actions as "proper and necessary" implementation of the other powers assigned to the Congress by the Constitution; among them, the power "to lay and collect taxes, . . . to pay debts, and provide for the common defense and general welfare of the United States; . . . to borrow money on the credit of the United States; (and) to regulate commerce. . . ."

The earliest monetary statute, the so-called "Mint Act" of April 2, 1792, established that "the money of account of the United States shall be expressed in dollars or units" and that principal subsidiary parts of the dollar be expressed in "disimes *(sic)* or tenths, cents or hundredths, and milles or thousandths" and that "all accounts in the public offices and all proceedings in the courts of the United States shall be kept and had in conformity to this regulation." By this action, the United States became the first of the present community of nations to adopt the decimal system for its currency.

The choice of the dollar as the principal unit of United States currency was largely through the influence of two men: Alexander Hamilton, the first Secretary of the Treasury, and Thomas Jefferson, the first Secretary of State. In memoranda dated 1791, Jefferson wrote: "In fixing the unit of money, these circumstances are of principal importance: 1. That it be of convenient size to be applied as a measure to the common money transactions of life. 2. That its parts and multiples be in an easy proportion, so as to facilitate the money arithmetic. 3. That the unit and its parts or divisions be so nearly of the value of some of the known coins, as they may be of easy adoption by

the people. [As a model] the Spanish dollar seems to fulfill all these conditions."

"The expediency of attending to the size of the money unit," Jefferson added, "will be evident to any one who will consider how inconvenient it would be to a manufacturer, or merchant, if, instead of the yard for measuring cloth, either the inch or the mile had been made the unit of measure."

## How the dollar got its name

Although the dollar as a unit of currency came to the American continent in the form of Spain's *peso de 8 reales* (the storied "piece of eight"), the name itself originated with a large silver coin called the *Joachimsthaler* which made its appearance about 1518 at a Bohemian mint located in the valley (or *thal*) of St. Joachim. *Thalers* rapidly gained favor throughout Europe; and the name, modified according to the speech of individual countries became *daalder* in Holland; *daler*[1] in Scandinavia, and *dollar* in England. The word appears at least twice in Shakespeare's plays.

Over the years since the first United States dollar appeared, both the types and denominations of federal currency have changed many times. The first coins struck by the government of the United States, in fact, were not dollars but one-cent and half-cent copper pieces issued in 1793. They were about the size of today's half dollar and quarter. Other curiosities which have passed into history include two-cent, three-cent, and 20-cent pieces, a half dime, a $3 gold coin, and so-called "fractional" paper currency in denominations ranging from three to 50 cents. Other paper currency that has circulated in the nation within comparatively recent times includes national bank notes, Treasury notes of 1890, gold certificates, and silver certificates.

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1. One of the dollar's European ancestors holds the distinction of being the largest metallic coin known. In 1644, Sweden used 10-daler pieces weighing 38.5 pounds. They were rectangular copper slabs measuring 12 x 24 inches.

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## Legal tender

Although none of these are issued by the United States today and most are found only in numismatic collections the Congress has provided that "all coin and currencies of the United States . . . ; regardless of when coined or issued, shall be legal tender for all debts, public and private, public charges, taxes, duties, and dues." A three-cent demand note of 1864 (the smallest paper currency ever issued by the federal government) or a $10,000 Federal Reserve note (the largest denomination[2] ever used as circulating currency) are still lawful money.

Under present laws, only the Treasury and the Federal Reserve System may issue United States currency. The Treasury issues all coin and that type of paper currency known as United States notes. Under the Act of May 31, 1878, some $323 million in these notes must be kept outstanding. They are now issued in denominations of $100 only. Formerly $1, $2, and $5 notes were issued. The Treasury seal and serial number on these notes are in red.

## Currency in circulation

The rest and by far the largest proportion of currency now issued is in the form of Federal Reserve notes. At the start of 1978 these comprised almost nine-tenths of the nation's "currency in circulation" some $93.1 billion out of a total of $103.8 billion. The remainder included $10.1 billion in coin (about 10 percent), $316 million in United States notes (less than 1 percent), and $280 million in currencies no longer issued.

Seven denominations of Federal Reserve notes - $1, $2, $5, $10, $20, $50, and $100 - are being furnished to banks for circulation. Since July 14, 1969, larger denominations of

2. The largest denomination issued $100,000 gold certificate of 1934 was designed for official transactions only and has never circulated outside Federal Reserve Banks. Twelve were outstanding on December 31, 1977 (five in the Federal Reserve Bank of Atlanta, two in New York, one in Philadelphia, and four in Kansas City).

$500, $1,000, $5,000, and $10,000 have been ordered retired. As with other currency no longer issued, these denominations remain legal tender but are being withdrawn from circulation when received by Federal Reserve Banks or the Treasury. The Treasury seal and serial number on these are in green.

The $2 note was reintroduced into circulation in 1976 to coincide with the nation's Bicentennial celebration. It had been discontinued by the U.S. Treasury in 1966 because of a lack of public demand. The decision to reissue the $2 note was based, in part, on the belief that the public would again find the denomination useful and convenient if it were issued in sufficient quantity. The use of $2 bills as a substitute for $1 bills would also reduce the cost of printing the nation's currency.

In July of 1979, the U.S. Mint released a new $1 coin, the Susan B. Anthony dollar, which is less expensive to produce and less cumbersome to use than the old Eisenhower dollar coin. In addition, substitution of the dollar coin for the dollar bill will result in savings to the Treasury. The $1 bill costs nearly 2 cents to produce and lasts only 18 months in circulation frequently in bad shape. The Susan B. Anthony coin costs 3 cents to produce and will last 15 years or more in good condition.

Physically, all United States paper currency has been of uniform size regardless of type or denomination since July 10, 1929. Prior to that date most issues measured 7.42 by 3.125 inches (although the three-cent "fractional" note was only 2.50 by 1.625 inches). Today all notes measure approximately 6.14 by 2.61 inches, are about .0043 inches thick, and weigh .03 Troy ounces. The design of both coin and paper currency, as well as the material used in its production, is determined by the Treasury.

## About the inscriptions

The denominational designs that individualize both our paper currency and coinage have varied

widely as federal currency has evolved. However, with the Act of July 11, 1955, the Congress instructed the Secretary of the Treasury to include the inscription "In God We Trust" on all United States currency, paper as well as coin. The following year the Congress adopted "In God We Trust" as the national motto. The inscription made its advent on a bronze two-cent coin in 1864; a coin subsequently discontinued in 1873. The inscrip- has been in continuous use on the one-cent piece since 1909; on the dime since 1916, and the nickel since 1938. The first notes to bear the inscription were $1 silver certificates paid into circulation on October 1, 1957. Today it is included in the design of all classes and denominations of currency.

All denominations of paper currency carry the Treasury seal. Prior to modernization of the design in 1968, it was encircled with the Latin *Thesaur. Amer. Septent. Sigil.*, an abbreviation of *Thesauri Americae Septentrionalis Sigillum*, meaning "The Seal of the Treasury of North America." The new seal bears the legend, "Department of Treasury" and "1789," the date the Treasury came into being.

Since 1935, the most familiar denomination of paper currency the $1 note has also carried the Great Seal of the United States on its reverse. The Latin inscription, *E Pluribus Unum*–literally, "Out of Many, One" appears on the Seal's obverse on the right. On the left, the Seal's reverse bears two inscriptions: *Annuit Coeptis*, meaning "He Has Favored Our Undertakings," and *Novus Ordo Seclorum*, meaning "A New Order of the Ages." *MDCCLXXVI* is the Roman numeral for 1776.

The new dollar coin carries the profile of Susan B. Anthony, an early crusader for equal rights for women. This is the first time that a portrait of an American woman rather than a symbolic woman has appeared on a circulating U.S. coin. On its reverse side, the coin depicts a symbolic eagle of Apollo 11 landing on the moon, a design which originally appeared on the Eisenhower dollar coin.

## How currency reaches the public

All paper currency and coin goes into and out of circulation through the Federal Reserve Banks or their branches. New coin is struck at the Bureau of the Mint's facilities in Philadelphia, Denver, and San Francisco. Paper currency is produced by the Bureau of Engraving and Printing in Washington, D.C. These last two bureaus are part of the Treasury, which also is charged by the Congress with enforcement of laws against counterfeiting. The broad responsibility for currency distribution, however, rests with the Federal Reserve System.

Federal Reserve machinery enables the public to convert bank deposits into cash, and vice versa, as dictated by the public's needs and demand. When people want more currency, they obtain it by drawing on their deposits at commercial banks. The banks, in turn, obtain their currency from the twelve Federal Reserve Banks or their branches. When people no longer want all the currency they have on hand, they deposit the excess in banks, and the banks subsequently deposit any excess with the Reserve Banks. This "elasticity" of the currency supply was a primary objective of the Congress when it passed the Federal Reserve Act in 1913.

## Why the amount of currency changes

The public's need for cash fluctuates and these fluctuations are frequent (and often substantial). The demand for pocket and cash register money varies for different days of the week, for different days of the month, and for different seasons. In agricultural regions the need for currency is heavy at times when crops are being harvested. Throughout the country, the need increases before holidays such as Easter, Labor Day, and Thanksgiving when many people take trips or for other reasons need more pocket money. There is an extraordinary increase before Christmas, when cash is used for Christmas shopping and as gifts. After

the holidays, excess currency is redeposited in the banks by merchants, hotel keepers, and others with whom it has been spent, and the banks in turn send it to the Reserve Banks.

In addition to seasonal changes in currency demand, there are changes that reflect variations in business conditions. When business activity is rising, the need for currency to make payments increases. When business activity slows down, the need for currency declines. Growth in population and changes in public buying habits also contribute to the changes in the supply of currency. (A proliferation in vending machines in the 1960's, for instance, caused a dramatic increase in the demand for coin.) It is such changes that the present currency system is designed to accommodate.

## The note issue mechanism

The issuance of Federal Reserve notes to a Reserve Bank is controlled by a special representative of the Board of Governors of the Federal Reserve System known as the Federal Reserve Agent. There is one agent for each of the twelve Federal Reserve Districts. A Reserve Bank must pledge with its agent collateral at least equal in amount to the notes outstanding from the bank.

This collateral may consist of legally specified assets, alone or in any combination, plus other financial assets that Reserve Banks may purchase or hold: (1) gold certificates; (2) direct obligations of the United States government (i.e., Treasury notes, bills, or bonds); (3) "eligible paper" as defined by statute, or (4) Special Drawing Right Certificates issued by the Secretary of the Treasury. The SDR certificates became lawful backing of Federal Reserve notes under an Act of June 19, 1968. The first issue to the System was certified on January 8, 1970.

Both gold and SDR certificates are issued only to Federal Reserve Banks, and they may not be placed in circulation. United States government securities are acquired by the Reserve Banks in open market operations, as directed by a special



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entity within the Federal Reserve System known as the Federal Open Market Committee.

The eligible paper component of allowable collateral may consist of short-term advances to member banks. An example of other pledgeable financial assets is foreign currencies held by Reserve Banks.

## How much cash is there?

On December 31, 1979, Federal Reserve notes issued to Reserve Banks and outstanding on the books of the Federal Reserve Agents amounted to \$125.3 billion, which included the \$113.4 billion in circulation and \$11.9 billion held in Federal Reserve Banks and the Treasury. The collateral pledged with the agents against these notes included \$11.1 billion in gold certificate credits with the Treasury; \$111.5 billion in United States government obligations; \$1.8 billion in SDR certificates, and \$894 million in eligible paper.

Aside from protection by collateral, the Federal Reserve notes are a first and paramount lien on all assets of the issuing Federal Reserve Bank. They are full obligations of the government of the United States. However, the liability of the federal government would arise only in the event of the liquidation of the Reserve Banks and then only to the extent that the collateral and remaining assets of the Reserve Banks were less than the amount of notes in circulation.

## Our de-centralized central bank

The twelve Federal Reserve Banks are situated in Boston, New York, Philadelphia, Cleveland, Richmond, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, Dallas, and San Francisco. There are branches in 25 other cities which process checks and handle currency and coin.[3] This geo-

3. Buffalo, Cincinnati, Pittsburgh, Baltimore, Charlotte, Birmingham, Jacksonville, Miami, Nashville, New Orleans, Detroit, Little Rock, Louisville, Memphis, Helena, Denver, Oklahoma City, Omaha, El Paso, Houston, San Antonio, Los Angeles, Portland, Salt Lake City, Seattle.

graphical distribution makes their facilities readily available to a representative cross-section of the national economy and at the same time assures their respective regions of appropriate representation within the Federal Reserve System.

## Who runs the Reserve Banks?

The Reserve Banks were organized and operate for the public service by authority of the Congress. They are under the supervision of the Board of Governors of the Federal Reserve System, an agency of the federal government. The seven members of the Board are appointed by the President of the United States, by and with the consent of the Senate and the Board is required by law to make annual reports to the Congress.

Each of the twelve Reserve Banks has nine directors, of whom three, including the chairman, are appointed by the Board of Governors in Washington. The other six directors, three chosen from non-bank businesses and three from banks, are elected by member banks. Salaries of all officers and employees and the appointments of the president and first vice president of each Reserve Bank are subject to approval by the Board of Governors.

## Who owns the Reserve Banks?

Unlike privately-managed commercial or savings banks, the Reserve Banks are not operated for the purpose of making profit. The stock of the Reserve Banks is held entirely by commercial banks that qualify as members of the Federal Reserve System. Ownership of that stock is a legal requirement of membership in the System and does not carry with it the attributes of control and financial interest ordinarily attached to stock ownership. This stock may not be sold, nor may it be pledged as security for loans. Dividends are fixed by law at 6 percent per annum.

Earnings of the Federal Reserve Banks are derived from interest received on their loans and securities, the volume of which reflects principally credit policies adopted in the public interest. All earnings are paid into the United States Treasury after the payment of expenses, the statutory 6 percent dividend to member banks, and any additions to surplus necessary to maintain each Reserve Bank's surplus at an amount equal to its paid-in capital stock. In 1979, these additions to surplus accounts amounted to $69.1 million; payments to stockholding member banks (required by law) totaled $67.2 million; and payments to the Treasury for the year amounted to $9,279 million. Between 1947 and 1979, payments to the Treasury totaled $73.1 billion. In the event of their liquidation, any surplus of the Reserve Banks, after meeting all obligations, would become the property of the United States government. □

Additional copies of "U.S. Currency" may be obtained by writing to: Publications Services, Board of Governors of the Federal Reserve System, Washington, D.C. 20551.